

Risk*topics*

managing vendor relationships

A large energy company faced an insured loss of nearly \$9 million—a loss that could not be recovered because there was a reciprocal waiver of liability in the drilling agreement. When the loss occurred, the insured also faced a \$100,000 rig deductible and another \$50,000 deductible that was not reimbursable because of these restrictions in the drilling contract. Don't make the same costly mistake.

When a state Board of Education entered into a large construction contract to expand its facilities, it reviews its contract carefully up front. One particular amendment the board requested proved critical: They eliminated a clause that waived subrogation, and instead revised the contract to permit subrogation to the full extent of the contractor's available insurance. As a result, they now expect to recover some \$3 million following a loss.

An often-overlooked area of property loss prevention is the contract you enter into with an outside vendor. Zurich North America Engineering can help you identify certain contractual "red flags" that need to be addressed to help ensure that when losses occur for which your vendor should be held liable, your vendor—the responsible party—will be.

Before you begin any vendor relationship, you should review, discuss, and negotiate the terms of your contract carefully. In the future, this may pay off with reimbursement of your out-of-pocket costs and can also lower your loss ratio because contract terms can improve Zurich's opportunities for successful recoveries against vendors who are responsible for losses.

In working with vendors, service providers, and contractors, whether your company is leasing equipment, purchasing supplies or making transit arrangements, keep in mind the following contract points:

- All vendors should submit Certificates of Insurance. Assess whether the coverage limits are appropriate. A rule of thumb for property coverage is 50 percent of the value of the property.
- All vendors should submit a contract outlining the scope of work to be performed.
- It may be in your best interest to strike the following provisions from the vendor's contract:
 - Limitations of liability. On contracts such as purchase contracts, the seller typically includes provisions that limit its liability. For example, the seller might specify that the only recourse you, the buyer, has in the event of a defect is repaired or replacement of the product by the seller, leaving the seller free from any other

liability related to the product.

- Indemnity provision. Contracts sometimes provide that your company agrees to indemnify a third party for damages caused by that third party. Although such contracts may be illegal in some states, in others this provision could force your company to indemnify a third party for their own negligence.
- Waivers of consequential damages. Your company may also enter into contracts stating the seller is not liable for indirect or consequential damages including loss of income or profits, increased costs of operation, or any other potentially foreseeable loss, whether a claim is brought in tort or under any other type of action.
- Waiver of subrogation. Often a company enters into contracts where both parties agree to waive all rights against each other for damages caused by fire or other causes of loss to property covered by property insurance, up to the policy limit.
- Statute of limitations. Often a company enters into contracts with provisions that prevent them from suing the other party after a specific time period. You should delete these limitations (whereby the statute of limitations in the given state would apply).

For more information

To learn more about how proper management of vendor relationships can help control your potential losses, contact your local Zurich North America Property team member or:

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